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France: Mitterrand's Nationalization Plans in Perspective

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A Research Paper

*Information available as of 16 June 1982
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This paper was prepared by [] Office
of European Analysis. Comments and queries are
welcome and may be directed to the Chief,
Western Europe Division, []

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**France:
Mitterrand's Nationalization
Plans in Perspective**

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Overview

The Mitterrand government elected last year has nationalized most French banks that had remained in private hands, two financial holding companies, and key firms in the steel, arms, chemicals, and electronics industries. In addition, Paris is negotiating for greater stakes in two firms that are largely foreign owned and has reached agreement on a third. In this wave of nationalizations, the government has twice revised its compensation formula upward; it must still resolve problems concerning divestiture of overseas affiliates and future management structures.

The nationalization program, which continues a long tradition of government economic intervention, plays a key role in the Socialists' overall plan to revitalize the economy. Nevertheless, it could lead to proliferation of economic activities that are not viable on their own merits. Businesses fear that the government would force nationalized firms to take economically unsound actions in an effort to reduce unemployment, and bankers have argued that it might pressure nationalized banks to extend credit injudiciously. A key measure of the program's success—and an issue likely to be raised by the opposition in the 1986 parliamentary elections—will be its direct impact on the economy. Voters will be trying to evaluate the nationalizations on the basis of their effect on unemployment, economic growth, and inflation.

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The program may affect the management of previously private French holdings in the United States as well as US shareholdings in French-based industrial companies and banks. Although Paris is likely to focus on improving the competitiveness of nationalized industries rather than risk retaliation through increased protectionism, policies favoring these industries will discriminate indirectly against foreign interests.

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A Long Tradition of State Control

The question of nationalizations is not the emotional, philosophical issue in France that it would be in the United States. Although Mitterrand's nationalization program is the first major cluster of government takeovers since former President de Gaulle nationalized France's three largest banks plus Renault, Air France, and the electric and gas utilities immediately after World War II, France has a long tradition of extensive government economic control. In past centuries, so much of France's wealth belonged to the state that private industry was forced to rely heavily on state patronage and accept state direction. One of Louis XIV's ministers instituted a system of strict and widespread regulation and direction of economic activity. In the 19th century, public capital was largely responsible for developing the railroads, mines, heavy industry, and the banking system.

The first big round of nationalizations came with the Popular Front government in the mid-1930s. The state purchased interests in shipping, armaments, and aeronautical concerns, set up a broadcasting system, and nationalized the railroads. Immediately following World War II, the need for speedy reconstruction inclined French Governments toward broad public ownership. Moreover, widespread criticism of wartime collaboration between big business and the Germans made a number of banks and industrial firms irresistible targets for takeover. Since the immediate postwar period, the government has acquired additional interests piecemeal.

Even after former President Giscard's economic liberalization policy, Paris dominated the financial system through its three big nationalized banks (Banque Nationale de Paris, Credit Lyonnais, and Societe Generale), the largely government-controlled specialized banks such as Credit Agricole, the large nationalized savings bank system (the *caisses d'epargne*), and three major insurance companies, (Union des Assurances de Paris, Assurances Generales de France, and Groupement des Assurances Nationales). In industry, the state sector included over 100 wholly or partially

government-owned firms and their more than 600 subsidiaries in such major industries as coal, oil, transport equipment, chemicals, and steel. (See table 1.)

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The performance of public firms generally has been good, but wide variation from company to company can be found. For example, Air France's operation of the Concorde has posted heavy losses, while wholly state-owned Renault has been a consistent money-maker. The relationship between the government and the state enterprises also has varied widely. While Renault managers have enjoyed near autonomy in formulating company strategy, the government has maintained closer supervision of Air France. In general, government influence over economic management has been largely indirect, having about as much effect on the private sector as the state sector. The major exception is that Paris often has used its weight in the public sector companies to force purchases from domestic suppliers. The most striking examples of this are Electricite de France's purchases of nuclear equipment from Framatome and Air France's purchases of the Concorde, which was built jointly by Aerospatiale, SNECMA, and the British.

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Public Attitudes

Most of the French readily accept the state as a key participant in the economy. Although many may disagree with specific government policies or with actions of individual bureaucrats, few question the basic notion of the state as a source of direction and dynamism. Thus, the concept of the public sector itself is not much of an issue. Nor do the French view nationalization of firms as a strictly leftist policy. Government officials, whether elected or in the civil service, are imbued with a strong tradition of center control. Neither they nor most of the public assumes that private enterprise is necessarily more efficient than state-directed enterprise.

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Monopolies	1980	
	Sales (Million US \$)	Employees (Thousands)
Postes et Telecommunications	13,519	459
Electricite de France	10,566	109
Societe Nationale des Chemins de Fer Francais	5,700	252
Charbonnages de France	3,340	79
Gaz de France	3,617	28
Regie Autonome des Transports Parisiens	1,074	37
Service des Tabacs et Allumettes	552	10
Competitive Firms		
Renault	13,351	232
Elf Aquitaine	12,784	49
Air France	2,476	33
Aerospatiale	1,978	34
Societe Nationale d'Etude et de Construction de Moteurs d'Aviation	863	20
Total	69,820	1,342

Major Nationalized Banks

	1980		
	Assets/Liabilities	Profits (Million US \$)	Employees (Thousands)
Banque Nationale de Paris	89,376	166	47
Credit Lyonnais	81,517	115	45
Societe Generale	74,938	184	34
Total	245,831	465	126

Major Nationalized Insurance Firms

	1980		
	Income from Premiums	Profits (Million US \$)	Employees (Thousands)
Union des Assurances de Paris	7,289	70	30
Assurances Generales de France	1,510	24	13
Groupement des Assurances Nationales	1,349	26	8
Total	10,148	120	51

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Significantly, top private managers and high-ranking civil servants—graduates, for the most part, of the same elite state schools—have no difficulty moving among jobs in the government and in the public and private industrial sectors. In the French view, this “revolving door” tradition adds an element of stability and continuity to the economic system. Despite its leftist orientation, the Mitterrand government is no exception to this pattern. Industry Minister Pierre Dreyfus, for example, was president of Renault for 20 years; the new head of recently nationalized Thomson Brandt left the civil service to direct Saint-Gobain in 1970. Indeed, the majority of presidents of the newly nationalized firms are former high civil servants in the “old boy network” tradition. []

In a recent public poll over one-half of the respondents favored the government’s nationalization program, while 29 percent opposed and one-fifth were undecided. Opponents included industrialists, bankers, and people resistant on economic and ethical grounds. The top executives of the newly nationalized industrial firms fear that the government—in a costly bid to limit France’s rising unemployment—could go beyond a shuffling of top management and force nationalized firms to carry unneeded workers and undertake or prolong unprofitable activities. They also have said that the nationalization of French-based multinationals could put a check on the “internationalization” of France’s industrial groups. Restrained from expanding production abroad in search of cost advantages, companies supposedly would seek larger shares of the home market. The result could be increased protectionism—a course denied by Paris—which would invite retaliation. []

Similarly, the heads of the banks affected by Mitterrand’s nationalization policy have argued that the government, despite its disclaimers, might interfere unwisely in the management of their institutions. Banks could be pressured into extending credit to firms in financial difficulty—particularly small- and medium-size firms—without regard for the creditworthiness of borrowers or the soundness of their projects. []

Political opponents of the Mitterrand government have misgivings over the cost of compensating the owners of nationalized firms and the inflationary implications of the compensation payments and the promised increase in investment by the expanded state sector. They argue that competition will be reduced, with a resultant loss of efficiency and increases in costs and prices. [] 25X1

In their policy statements, Socialist leaders have clearly indicated that the nationalizations are part of a restructuring plan for the industrial sector that is aimed at increasing national self-sufficiency and international competitiveness. According to Mitterrand and other spokesmen, the nationalizations are meant to relieve a few private industrialists of control over domestic distribution and prices while ensuring that this control will remain in French hands. The nationalization plan includes measures to increase worker participation in decisionmaking. Expanded state control is supposed to facilitate government plans for the economy, which in the past have been mainly indicative in nature. [] 25X1

The Nationalizations at a Glance¹

The new Socialist government moved swiftly to negotiate nationalization agreements with the steel and arms industries last fall and to push through final 25X1 legislation on the takeover of several banks, two financial holding companies, and five major industrial groups earlier this year. Negotiations for two key foreign-owned firms are under way, agreement on a third was recently reached. (See table 2.) []

With the new legislation, the government has doubled its share of the industrial sector to about 30 percent. The state owns 66 percent of the nonferrous metals industry, compared with 16 percent before; 52 percent of basic chemicals, compared with 16 percent; 42 percent of electronics, from virtually nothing; 37 25X1

¹ Even though the nationalizations went into effect in 1982, the data used in this section are based on 1980 financial figures, which represent the latest information.

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percent of glass products, from nothing. It has increased its control of the steel and armaments industries and is the direct employer of about 2.1 million workers (23 percent of all industrial workers), compared with 1.3 million (14 percent of all industrial workers) before the new legislation. In 1980 the newly nationalized French-owned concerns posted combined sales of about \$43.7 billion and employed about 770,000 people, 200,000 of whom worked outside France. The foreign-owned concerns had sales totaling \$2.4 billion and employed some 50,000 workers, about 11,000 of them outside France. (See figure 1.)

The nationalization of 36 private banks and three cooperative banks, plus the takeover of minority shares in three seminationalized banks, adds 13.4 percentage points to total bank deposits and 15.4 percentage points to credits to public sector institutions. The private sector still includes roughly 70 French and 150 foreign-owned banks—but these account for only 3.2 percent of deposits and 7.4 percent of loans (See figures 2.)

Details by Sector

Banking. Nationalization extends to all registered commercial and merchant banks having deposits of at least \$175 million. Paris has also nationalized three cooperative banks, Banque Centrale des Cooperatives et des Mutuelles, Banque Federative du Credit Mutuel, and Banque Francaise du Credit Cooperatif. Foreign minority shareholders in nationalized banks may choose either to keep their holdings or sell them to the government. The banks exempt from takeover are those whose capital is “directly or indirectly controlled” by foreigners, those specializing in real estate, and rediscount houses. While the new laws do not directly nationalize any insurance firms, state ownership of the insurance industry has been expanded because the newly nationalized banks are prohibited from divesting themselves of insurance company stock.

The five major banking concerns affected include two financial holding companies, Banque de l'Indochine et de Suez (IndoSuez) and Banque de Paris et des Pays Bas (Paribas); and three banking groups, Credit Industriel et Commercial, Credit Commercial de

France, and Credit du Nord. These banks combined accounted for about 12 percent of the assets of all registered banks in 1980, compared with about 48 percent for the big-three previously nationalized banks. The five groups, which are characterized by complicated financial structures, have important industrial holdings and extensive foreign networks in branches, subsidiaries, and affiliates. Some of the industrial shareholdings will be sold to the private sector, but Paris will probably retain holdings in firms it considers to be of “national importance.” Paribas' interests in the electronics firm Thomson-CSF would fall into this category. Paris had already taken steps to keep Paribas' interests in the specialty steel firm Creusot-Loire and the nuclear plant construction firm Framatome.

Government officials have made clear their intention to restructure the banking system but have given only a few clues about the nature and timing of such a move. Prime Minister Pierre Mauroy has stated that the banking sector will remain pluralist and that businessmen will retain the right to choose and change bankers. He has indicated further that the government will establish regional bank councils and regional banks “of a new kind” to better meet regional needs for credit. According to Mauroy, the regional networks are intended to reduce the decision-making power of Parisian bank offices. However, the Prime Minister states that the regulatory powers of the Conseil National du Credit (the interministerial body that determines credit policy and bank practices) and the Commission de Controle des Banques will be expanded to include authority over all credit institutions, regardless of category. Beyond strengthening the Conseil and Commission, the extreme view within the Socialist Party calls for creation of an Office of Nationalization to handle regionalization of the financial system.

The roles of the money market and international operations of banks following nationalization must still be resolved. Hardliners within the Socialist Party favor the establishment of a National Investment

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Table 2

France: Mitterrand's Nationalization Plan

Competitive Firms	1980		
	Sales (Million US \$)	Profit (Million US \$)	Employees (Thousands)
Compagnie Generale d'Electricite	8,428	103	180
Saint-Gobain	8,002	167	164
Pechiney-Ugine-Kuhlmann	7,013	112	90
Thomson-Brandt	6,716	93	128
Rhone-Poulenc	5,520	- 350	95
Usinor	3,128	- 221	34
Dassault	1,976	58	16
Sacilor	1,855	- 357	17
CII-Honeywell-Bull ^a	1,159	33	20
Matra ^b	1,030	39	45
Roussel-Uclaf ^a	975	24	18
Compagnie Generale de Construction Telephonique ^a	307	- 26	10
Total	46,109	- 325	817
Major Banks (1980)	Assets/Liabilities		
Banque de l'Indochine et de Suez	47,916	161	36
Banque de Paris et des Pays Bas	43,794	240	29
Credit Industriel et Commercial	23,737	41	5
Credit Commercial de France	12,421	35	7
Credit du Nord	8,023	17	12
Total	135,891	494	89

^a Firms with major foreign interests.^b Press and other media-related activities are excluded from takeover; they will be split under a new holding company, tentatively called Matra-Medias.

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Bank to direct long-term credit allocation and propose that the free interbank market be replaced by total reliance on the Bank of France for bank liquidity needs. The future international function of banks is highly uncertain. In recent years, French banks have followed a policy of rapid international expansion aimed at providing banking services for French exporters and overseas investors. The banks expanded their overseas activities so rapidly because lending in France was limited by credit controls. According to

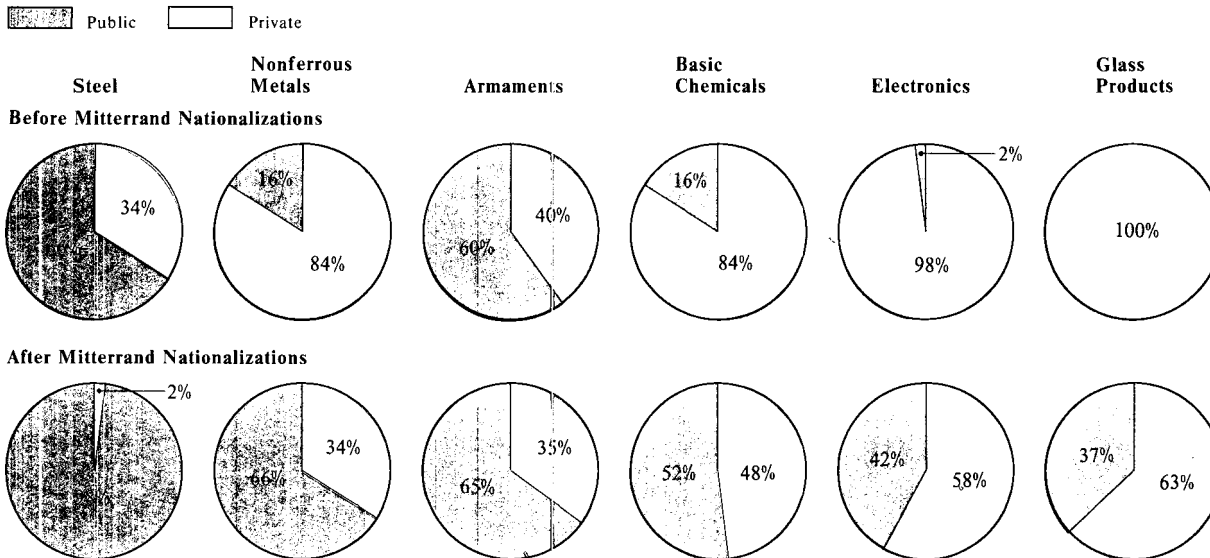
the US Embassy in Paris, however, the new government plans to reduce incentives for overseas lending and divert the focus of banking activities inward.

Socialist spokesmen, such as Mauroy, State Secretary Le Garrec, and Finance Minister Jacques Delors, have argued that monopolization of credit distribution will enable the government to "integrate" credit allocation into its plans for restructuring the economy.

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Figure 1
French Industrial Sector (by production), 1980^a



^a Even though the nationalizations went into effect in 1982, the data used in arriving at percentages are based on 1980 financial figures, which represent the latest information available.

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Behind this argument lies the frequently expressed notion that the banks have been profiting at the expense of industry. According to this view, the banks have not lived up to their social responsibilities in providing credit to firms in financial difficulty, preferring more profitable but "nonproductive" investments. In addition, Socialist "reform" clearly implies a redirection of capital for investment from the multinationals to small- and medium-sized firms.

Arms Industry. The government has signed nationalization agreements with two industrial groups in the arms industry, the large aircraft and missile group Dassault-Breguet and the armaments and high technology group Matra. The agreement signed with Dassault transferred 26 percent of the company's stock to the government, which already held 20 percent. The government now holds 46 percent; it intends to purchase the remaining 54 percent by the

end of 1985. To ensure continuity within the company, Paris agreed to retain management and other key personnel and to leave intact existing departments such as research and development, commercial, and technical divisions.

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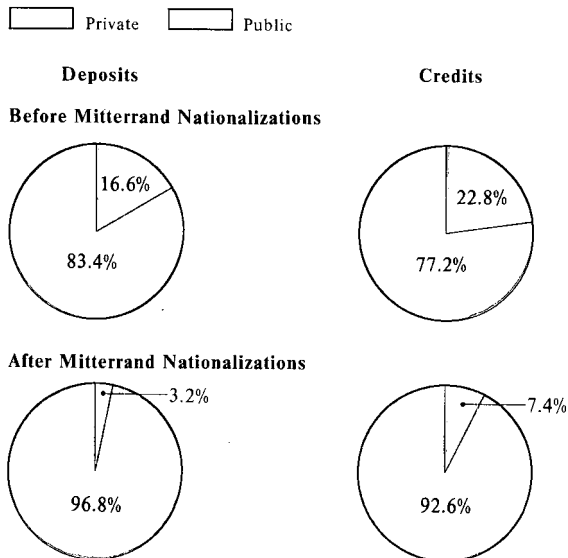
The agreement signed with Matra will eventually turn over 51 percent of the entire group's shares to the state. Only Matra's media-related companies will be excluded from the takeover. At the urging of Matra's chairman, who feared that the group's newer and currently less profitable ventures into electronics, optical equipment, and clockmaking could not stand on their own, the government departed from its plan to nationalize only Matra's aerospace and armaments division, which accounts for just half its sales but 90 percent of its profits. Still to be announced are methods for handling government purchases of stock and compensation terms. Matra's press and other

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Figure 2
French Credit Sector, 1980^a



^aEven though the nationalizations went into effect in 1982, the data used in arriving at percentages are based on 1980 financial figures, which represent the latest information available.

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media activities will be split off under a new holding company, tentatively called Matra-Medias, that would be spared from nationalization. This company will own 20 percent of Marlis—which in turn holds 75 percent of the Hachette publishing empire—60 percent of Haussmann-Gestion, and 16 percent of Europe l'Image et Son, a radio and television holding company. 25X1

After Matra's partial nationalization, the structure of the board of directors will change. The government will appoint half the board, and private shareholders the other half. The current managing director will probably remain and be given greater than normal power, particularly for occasions when the board is deadlocked; he is expected, along with other key personnel, to continue to manage Matra-Medias. Legislation may still have to be submitted to legalize these arrangements. Moreover, according to press reports, the unions, the Communist Party, and more radical Socialist deputies in the National Assembly may fight the government's plan, hoping to nationalize all of Matra's holdings. 25X1

The heads of Matra and Dassault were pleased that they were able to negotiate terms that maintained company integrity. At the same time, the Mitterrand government had strong reasons for accepting the terms. In Dassault's case, Paris realized the importance of keeping the highly skilled Dassault team intact; with Matra, the government accepted the argument that the weaker manufacturing companies could not survive on their own and that the state should not control the media. The attempt to keep the Dassault team together, however, may prove futile. Several senior managerial people have reportedly announced that they will resign by the end of 1982, citing "government interference" in management as the cause. 25X1

Steel Industry. Even before Mitterrand came to power, Paris held controlling interest in the two major steel groups, Usinor and Sacilor, which comprised 80 percent of the steel sector. By converting to stock about \$2.5 billion in loans owed the state by the two ailing companies after the financial reorganization of 1978, the government has increased its interest in the industry from 66 percent to nearly 98 percent. The government recently approved the merger of the specialty steel firm Ugine-Aciars into Sacilor. This merger—coupled with that of Creusot-Loire and Usinor—will complete the creation of two integrated groups, each capable of producing a wide range of steel products. 25X1

Still to be debated is the further "restructuring" that the Mitterrand government has planned for the steel industry, including the possibility of greater "cooperation" between Usinor and Sacilor. The two groups posted a combined loss of about \$580 million in 1980. Restructuring the steel industry and restoring it to international competitiveness clearly is difficult given the current situation in the world steel market, but much had already been done in terms of reorganization and cuts in the work force as part of Giscard's steel restructuring plan. While the present government plans to double annual investment expenditures to about \$850 million, further cuts in capacity and employment are likely. 25X1

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Industrial Groups

Five diversified industrial firms have been completely nationalized: Compagnie Generale d'Electricite (CGE) and Thomson-Brandt, electrical and electronics groups; Pechiney-Ugine-Kuhlmann (PUK), which produces chemicals and metals; Rhone-Poulenc, chemicals, textiles, and pharmaceuticals; and Saint-Gobain-Pont-a-Mousson, a diversified industrial conglomerate producing glass containers and electronics components. All but Rhone-Poulenc posted profits in 1980. As anticipated, only the parent companies of these giant industrial groups have been directly taken over, although nationalization of the parent companies has given the state controlling interests or important minority shares in a vast network of subsidiaries and affiliates. Foreign owners of stock in subsidiaries will be given the option of retaining or selling their shares. []

- CGE is France's largest electrical and electronics group and one of the 10 largest electrical machinery equipment concerns in the world. One-third of its 1980 sales of \$8.4 billion were exports. Domestically, it heads most of the sectors in which it operates, and it is a world leader in high-voltage electrical equipment, underwater cables, and, through its subsidiary CIT-Alcatel—France's telecommunications specialist—digital switching systems. Rapid diversification since the 1960s has brought in Alsthom-Atlantique, with its nuclear, engineering, rail, and shipbuilding interests. In addition, CGE has invested in construction equipment, and office equipment.
- Thomson-Brandt, the electrical, electronics, and arms group, includes over 100 companies and about 200 production plants, 30 of them outside France. Last year, overseas activities accounted for 45 percent of its sales. The company was formed late in the last century as the licensee of the Thomson Houston Electric Corporation, an American firm. The last US shareholding interests pulled out in the 1950s, and in 1966 the firm merged with the Hotchkiss Brandt armaments group. State entities already held over 10 percent of the capital. []

- PUK, the metals and chemicals group, is France's largest exporter to Japan and has a big foothold in the United States through its Pucko subsidiary. It relies heavily for profits on foreign activities, including technology sales; exports accounted for over half its \$7 billion of sales in 1980. Consolidated net earnings fell nearly 40 percent in 1980 to \$14.2 million. Only aluminum and fine metals, including nuclear fuel, were in the black. The Socialists plan a drastic restructuring of PUK's chemical, aluminum, nuclear, and steel divisions.
- Rhone-Poulenc, France's largest chemical company, also is undergoing a radical restructuring. It has sold its heavy chemical interest—accounting for one-third of sales in 1980—and is currently pushing through draconian cuts in its artificial fibers division. The thrust of its present strategy is toward a greater emphasis on processed chemical products, such as animal food additives, veterinary products, engineering plastics, rare earths used to color plastics, and silicones. Crippling losses in its textiles division have resulted in a sharp slump in overall earnings.
- Saint-Gobain has interests in glassmaking and steel pipe, where it ranks among the foremost world producers, and in insulation material, in which it is rapidly expanding because of energy conservation programs. About half of its \$8 billion worth of sales in 1980 were exports. The company answered Giscard's call for industry to push into high-technology sectors with a series of bold acquisitions in computers and computer-related fields. It has diversified into semiconductor manufacturing, has become the majority shareholder in CII-Honeywell-Bull, and now holds a 30-percent share of Olivetti, the Italian office equipment company. []

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Dealing With Foreign Interests

As an adjunct to efforts already under way, the government is pushing to increase its stake in two companies that are largely foreign owned: France's

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second-largest pharmaceutical producer, Roussel-Uclaf (58 percent West German owned) and the ITT subsidiary, Compagnie Generale de Construction Telephonique (CGCT) 99 percent US owned. Earlier this year, the government increased its stake in France's largest computer builder, CII-Honeywell-Bull (CII-HB, 47 percent US owned). []

- Roussel-Uclaf, the pharmaceuticals group, has been a subsidiary of West Germany's Hoechst since 1974. It comprises some 80 French and foreign companies; 60 percent of its sales are overseas, mostly through local subsidiaries. In addition to pharmaceuticals, it has interests in agricultural and veterinary products and in perfume. Last September, Bonn urged Paris to provide prompt and adequate compensation. In the meantime, the Germans have been reviewing legal aspects of the matter in light of France's obligations as a member of the European Community. []
- ITT in France, made up of subsidiaries of US-based ITT, has been reduced sharply in size in recent years. Thomson-Brandt bought its telephone interest, Le Materiel Telephonique, in 1976. ITT has also sold a private education subsidiary and, more recently, its television company, Oceanic, and its interests in electrical lighting equipment, cosmetics, and car radios; CGCT is the main operation left. Paris would like CIT-Alcatel, a key subsidiary of CGE, to buy a 51-percent share in CGCT. ITT would prefer to keep only 25 to 30 percent but reportedly would accept 34 percent. Valuation, method of payment, and access to ITT technology remain to be settled. Paris apparently wants a quick and equitable agreement that will keep CGCT running and avoid any conflict with Washington. []
- CII-HB, controlled by Saint-Gobain, has been heavily financed by the state for several years. The government hopes to build a large and dynamic computer industry around CII-HB and agreed last April to pay the US firm Honeywell \$150 million to acquire 27 percent of its interest in CII-HB. Honeywell now retains a shareholding of just under 20 percent of the computer concern but maintains long-term commercial and technical agreements with CII-HB. []

Compensation

The valuation formula to be used for compensation of the parent companies, the two financial holding companies, and the banks quoted on the stock exchange has been twice revised. In the first instance, to mute criticism that companies had been undervalued, the government backed away from a formula based solely on three-year (1978-80) average stock market quotations. Instead, it adopted a weighting scheme based 50 percent on the three-year average, 25 percent on such balance sheet items as capital and reserves, and 25 percent on 10 times the average annual net profits over the three-year period. This decision increased compensation by varying amounts. []

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In the second instance, French officials responded to a ruling by the Constitutional Council that valuation still was inadequate. Under the new plan—which will raise the cost of the nationalization from \$6 billion to about \$7 billion—shareholders of the nationalized concerns will receive the highest average share price, adjusted for inflation, over the six-month period ending March 1981. To make up for nonpayment of dividends in 1981, stockholders of the nationalized firms also will receive a bonus equivalent to the dividends paid on 1980 earnings plus an adjustment for inflation. A special committee will handle compensation to stockholders of banks whose shares are not publicly traded. These 21 banks are scheduled to be nationalized in January 1983. []

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There was earlier speculation among French officials involved in drafting the nationalization legislation that stockholders would be given a choice between purely "financial" bonds (bearing semiannual interest equal to the rate established for state obligations in the secondary market) and a "participatory" bond (return based partly on a percentage of the company's after-tax profits). Although the government opted for issuing only the former as compensation at this time, the nationalization bill explains that Paris may introduce participatory bonds in legislation. []

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Divestiture of Holdings Abroad

The disposition of overseas subsidiaries, affiliates, and joint ventures remains to be worked out. In the end, the government may or may not direct companies to divest themselves of some of their considerable foreign interests. The government reportedly wants PUK, for example, to keep its wholly owned US subsidiary, Howmet Turbine Components Corporation (defense contracting). However, the government clearly will allow divestiture of foreign subsidiaries, branches, and shareholdings if required by foreign law. []

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The two investment banks, Paribas and IndoSuez, are required to divest themselves within a year of shares in companies not involved in banking or insurance (except for holdings in industrial and commercial companies that already are targeted for nationalization). The French Government will examine case by case the overseas holdings of the two groups to determine which companies should be divested. Former shareholders in the two financial holding companies will be given priority in purchasing shares when any such divestitures occur. []

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Management Structure

The French cabinet approved a list of top managers for the newly nationalized entities last month; it also confirmed new leadership for the previously nationalized banks. With the exception of the heads of Saint-Gobain and Rhone-Poulenc, all top managers of recently nationalized entities are new; most have some connection either to the organization which they will head or at least to its principal branch of activity. None of the appointees, with the exception of the new head of Credit Lyonnais, has played a prominent role in the Socialist Party. The appointments and the naming of a non-Socialist career civil servant to the number-two position in the Ministry of Finance suggest that French officials wish to convey a signal of competence and continuity. Mitterrand's message accompanying the appointments stated with some ambiguity that the new elements of the nationalized sector "must not be appendages of the government" but should be "completely autonomous with the necessary controls exercised only after the fact." []

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The mode of operation of the newly nationalized concerns is still to be defined. Boards of directors of the companies and banks will consist of representatives from the government, the companies and banks, labor, and private individuals selected on the basis of familiarity with the respective industrial or financial activities. All board members will be appointed initially for three years; six-year terms will follow. Paris has indicated clearly that for major policy issues—decisions on acquisitions, divestitures, and borrowing—board members representing the state will have ultimate authority. []

The nationalization bill indicates that the government plans to introduce legislation at a later date on the "organization and democratization" of national enterprises. Meanwhile, appropriate ministries will provide direction to managers to facilitate negotiations with the unions for greater worker participation. Government spokesmen have stated that the nationalized firms will in a sense be "social laboratories"; specific measures will be laid out in a "social innovation" law that will embody principles of "self-management" (*autogestion*). []

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Nationalization, Industrial Structure, and Planning

The principal criteria used by the Socialists to determine which industrial groups to nationalize stem from long-held beliefs that Paris should control those industries fundamental to national economic development, "strategic" to national security, or resistant by reason of their size to indirect government influence. If these companies were not nationalized, they would, in Mitterrand's words, become rapidly "internationalized," subject to "an international division of labor decided far away, obeying interests" which are not those of France. But if they are nationalized, the Socialists argue, state control will enable French industry to "reconquer" the domestic market and will improve the international competitiveness of such industries as telecommunications, electronics, and pharmaceuticals. The Socialists maintain that the steel and chemicals industries are basic to national economic development and that the arms and aircraft industries are clearly strategic. [redacted]

The Socialists believe that the newly nationalized groups previously were structured to garner excessive profits, evade taxes, and concentrate power in the hands of a few. In their view, the webs of holding companies, subsidiaries, and sub-subsidiaries that make up most of the newly nationalized groups were based on no industrial logic and ought to be simplified. In their view, each group should handle all stages of production involved in manufacturing a product—from raw material to finished form. [redacted]

In restructuring PUK, for example, subsidiaries involved in the production of aluminum will be put together to form a separate, autonomous entity. The PUK chemical division, on the other hand, which is not an industry leader, will be attached to already-existing public groups, while the PUK specialty steel firm, Ugine-Aciers, is to be part of the Sacilor group. The PUK nuclear division would go to the French Atomic Energy Commission (CEA) and the state-owned General Nuclear Materials Company (COGEMA). Paris had already moved in this direction last fall when it increased the CEA share in Framatome. The government plan for restructuring the nuclear industry calls for an eventual regrouping of Framatome, Electricite de France, and Alsthom-Atlantique. [redacted]

In the aerospace sector, the government has indicated in its industrial policy statements that it plans closer coordination between the aircraft activities of Dassault and the National Aerospace Industry (SNIAS) as well as between the satellite and missile activities of Matra and SNIAS. In telecommunications and electronics, the resources of two existing big firms, Thomson-Brandt and CIT-Alcatel (and probably CII-HB), will be combined; employment is to be maintained. Restructuring in the fine chemicals industry will entail pooling the research programs of Rhone-Poulenc and the other laboratories (Roussel-Uclaf, Sanofi, Pharmaka). Major investment programs will be launched in all these areas. [redacted] 25X1

A mixture of financial incentives and public directives is to be developed to create internationally competitive companies in such ailing industries as machine tools, textiles, toys, leather, and furniture. In addition, the Socialist government would favor the development of new industries in sectors where France seems to have some technical advantage or export potential, such as electronics, information processing, and telecommunications. [redacted] 25X1

Since the fundamental goal of industrial planning is a different allocation of resources, privileged financing will probably accompany these efforts. Nationalizing credit gives the government the means to implement industrial policy by directing capital to investments that are in line with national objectives. Credit can be directed toward favored purposes, and industrial investment can be stepped up. Indeed, Paris recently announced the objective of increasing spending on research and development from 1.8 percent of GNP currently to 2.5 percent by 1985. To this end, the government has allocated \$8.6 billion for research in 1982, representing an increase of about 37 percent over last year. This accounts for about three-fourths of the total French R&D effort—about \$13 billion in 1982—including the expenditures of the newly nationalized firms. The level had previously been two-thirds. The government will also boost the R&D budget by nearly 18 percent in real terms in each of the next three years. In addition, the government has called for industry, led by the nationalized sector, to

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increase its expenditures on research and development. It is currently considering financial incentives such as tax allowances for research. []

The Socialist industrial plan rests heavily on belief that the government can intervene effectively both to set priorities for industry and to provide an environment in which companies can develop. Planning is part of the Mitterrand government's effort to "reconquer" the domestic market, render France more self-sufficient, and push exports through a program of research innovation, and investment. Although the Ministry of Planning and Regional Development has not yet completed its comprehensive Five-Year Plan (1984-88), it has announced a two-year (1982-83) interim plan, aimed at pulling France out of recession. Specific objectives include:

- Boosting real GNP growth to 3 percent annually compared with just 0.7 percent last year, primarily through increased investment.
- Shaping the composition of growth through the allocation of public sector financing.
- Reducing unemployment, currently at 8.6 percent, through job creation and further reduction of the workweek.
- Protecting worker purchasing power by controlling inflation, currently at 14 percent and likely to rise. []

US Concerns

The nationalization program will directly affect US involvement in CII-HB and ITT-France; US shareholdings in French-based parent companies, subsidiaries, and banks; and previously private French holdings in the United States. The direct involvement of US firms in the parent companies or major subsidiaries of the newly nationalized firms other than CII-HB and ITT-France is relatively small. Westinghouse is potentially involved because of its 10-percent share in the nuclear firm Framatome. Joint ventures in France between targeted companies and US firms include Eurotechnique (Saint-Gobain and National Semi-Conductor), Matra-Harris, and a Matra-Harris joint venture with Intel. []

In the credit sector, because branches or affiliates of US banks will not be nationalized, the major issue will be whether the postnationalization banking environment will discriminate against established US banks.

Although Jacques Delors has stated that the government will not take measures against foreign-owned banks, changes stemming from the virtually total nationalization of the credit sector could affect them indirectly, for example, in franc lending and in the autonomy of local banks with which foreign banks work. Moreover, the functioning of the money market could change in ways that would make it more difficult for foreign-held banks to borrow francs. Because nearly all foreign banks have more franc credits than deposits, they depend more than French banks on the money market for funding. The current central bank policy of keeping the prime rate several points below the money market rate—a reversal of the normal relationship—could hurt profits if it were continued over the long term. Although the policy is not aimed specifically at foreign-owned banks, the potential consequences for them are serious. []

Nationalized banks with minority US ownership may be pressed to allocate a greater portion of their loans to government-favored higher risk customers, with an attendant decline in profitability. The logic of this flows from the Socialists' belief that the banks have failed to give adequate support to firms in financial difficulty. US financial companies that would be affected include Wells Fargo Bank (15 percent of Credit Chimique), Harris Savings and Trust (5 percent of Hervet), INA Corporation (5 percent of Indo-Suez), Aetna Life (4.4 percent of Rothschild), Transamerica (20 percent of Compagnie Europeene de Banque), and Famille Steiner-Heilpen (12.5 percent of Banque Commerciale Privee). []

French Investment in the United States

Some of the newly nationalized French companies have significant holdings in the United States, mostly in the form of direct investment achieved by takeovers. Among these holdings are Howmet Aluminum and Howmet Turbine Components Corporation, owned by PUK; two recently acquired petrochemical plants and several other subsidiaries owned by Rhone-Poulenc; Certain-teed, a manufacturer of insulation products, owned by Saint-Gobain; and Phoenix Steel and Refinement International, owned by Empain-Schneider. While such US subsidiaries are relatively

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small in dollar value, they could be important in individual instances—for example, the US defense contractor Howmet Turbine Components Corporation. At issue is whether the French Government will allow these US subsidiaries to be managed as autonomous profit-seeking units or whether investment and employment decisions will somehow be affected by French political and social considerations. []

Franco-US economic relations could sour if US business perceives the evolving French economic system to discriminate excessively against US and other foreign interests. The preferential financing that the Socialist government has said the nationalized banks will provide nationalized industrial companies is patently discriminatory and will be detrimental not only to US firms having subsidiaries in France but to any US firm whose products compete with the products of nationalized companies in any market. Similarly, the “buy French” policy that Mitterrand and other officials have promised for the expanded state sector will be harmful to US and other potential suppliers. Paris traditionally has discouraged foreign investment in France by imposing long delays for the screening of investment applications. We believe the Mitterrand government’s efforts to increase the nationalized sector’s share of the French market could include still higher barriers against foreign direct investment. []

In defending their program, Socialist spokesmen have stated repeatedly that its thrust is not isolationist. The Socialist program ostensibly would restructure and rejuvenate industries to improve their competitiveness rather than protect existing operations. French officials, such as Gerard de Margerie and Christian Giacomoto of the Finance Ministry, have noted that international links are essential because foreign trade and investment account for 25 percent of French GNP. To be sure, the Mitterrand government has been careful to exclude foreign-controlled banks from takeover and has shown willingness to resolve problems caused by foreign affiliates of nationalized firms—for example, in its special handling of Paribas and IndoSuez, with their many foreign interests. It has been flexible on the question of compensating foreign owners of nationalized firms. []

Outlook

Although the Mitterrand government has expressed the intention of preserving the autonomy and identity of the nationalized firms, Prime Minister Mauroy has stated that, for all their alleged independence, the nationalized companies will follow a “dynamic investment and employment policy” put forth by the government and that the public sector will become a “privileged area of social innovation.” This and other Socialist statements suggest that the government will go beyond an initial restructuring of components and shuffling of top management to guidance of decision-making in the nationalized companies, particularly toward increasing investment and raising employment. Statements about the banking sector indicate a clear intention to gear credit allocation more closely to the broad macroeconomic and specific industrial goals of the government. Thus nationalized companies apparently will routinely use preferential credits from nationalized banks to finance activities favored by government decisionmakers. []

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The Socialist strategy could result in particularly rapid expansion of the same high-technology industries favored by previous governments—for example, robotics, microchips, and telecommunications— [] although government spokesmen have vowed to use technology and increased investment to revitalize French industry across the board. A key facet of the strategy is the government’s plan to raise public and private spending on research and development. []

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Notwithstanding the stress on technology and investment, inefficiencies could develop in the expanded state sector because of preferential allocation of credit, government determination to boost employment, and subordination of the profit motive. Nationalized companies that are not viable on their own merits might survive and even expand. This would result in waste of resources and detriment to competing private firms, foreign and domestic, that must pay market rates for credit and earn a suitable return for their shareholders. []

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There are, however, political as well as economic limits to how much the government will be able to do with the nationalized industries without considering objective economic criteria. In the 1986 parliamentary election, voters will have a chance to evaluate the results of Mitterrand's entire effort to stimulate the economy and reduce unemployment. The employment of unneeded workers in the nationalized sector and increases in investment without regard to profitability will have some appeal, but over the next few years inefficiency in the nationalized industries could widen an already swelling public-sector deficit, spur inflation, and undermine France's international competitiveness, ultimately eroding voter support. Furthermore, desire to avoid retaliation against France's export industries should serve as a restraining influence on Socialist hardliners.

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